Supreme Court of the United States

No. 297. October Term, 1901

HARRY J. JAQUITH, Trustee in Bankruptcy of William S. FRANKLIN, Bankrupt, Appellant,

v.

CLARENCE W. ROWLEY et al.

BRIEF OF APPELLANT

Appeal from the District Court of the United States for the District of Massachusetts.

Statement of the Case

On November 8, 1899, Edwin F. Flanders and Emily W. Thayer alleging themselves creditors of William S. Franklin, the bankrupt, began separate actions through the same attorney, in the Superior Court of Massachusetts for the County of Middlesex, and on November 14, 1899, the writ was served by taking the body of said Franklin. Thereafter in order to secure his release, Franklin deposited with one

Joseph P. Silsby, Jr., two hundred and seventy-three dollars as security, whereupon said Silsby became surety on Franklin's bail bond which was conditioned to appear and answer to the suits (P. S. Mass., Chap. 163, Sec. 2,) as follows:

"Bail in a civil action shall be taken, as heretofore practised, by a bond to the sheriff, if the writ is served by him or his deputy, otherwise to the officer by whom the writ is served, with condition that the defendant shall appear and answer to the plaintiff, abide the final judgment of the court, and shall not avoid."

These suits were pending on Aug. 15, 1900, when Franklin was adjudicated a bankrupt, the appellant was appointed Franklin's trustee and qualified Sept. 21, 1900. At the first meeting of the creditors Clarence W. Rowley, attorney of record in the state court for both Flanders and Thayer, and a member of the bar of the United States Circuit and District Courts, appeared and proved the claim of Thayer for $150, and asserted a claim upon the whole $273 deposited with the surety. (Record, p. 5.)

October 18, 1900, said Rowley, upon behalf of both Flanders and Thayer, without leave of the bankruptcy court or notice to or knowledge of the trustee, took judgment by default in the suits in the state court. This did not come to the knowledge of the trustee until Jan. 18, 1901. Upon learning of it the trustee at once notified the surety not to pay the money over, (Record, p. 1) and at once in the name of the bankrupt petitioned the State Court to vacate the judgment and order the execution returned. (Record, p. p. 3, 4.) This the State Court denied, (Record, p. 5,) and thereupon the trustee filed his petition in the District Court of the United States for Massachusetts, setting out the facts and asking equitable relief against the appellees. This petition was denied Feb. 20, 1900, (Record, p. 7.) On the 28th of February, 1900, the District Court of the United States for Massachusetts granted a re-hearing, at which the Court permitted the trustee to amend his prayers for relief, the appellees appeared and denied the jurisdiction of the Court, and after argument the Court denied the petition for want of jurisdiction, and allowed an appeal to this Court. (Record, pp. 11, 15.)

FIRST AND SECOND ASSIGNMENTS

"That the final judgment denied the jurisdiction of this court to permanently enjoin a creditor of the bankrupt who has proved her debt in the bankruptcy court from collecting a judgment or levying an execution recovered in a State Court upon such debt."

"That the final judgment denied the jurisdiction of this Court to permanently enjoin a creditor of the bankrupt who has not proved his debt in the bankruptcy court from collecting a judgment or levying an execution recovered in a State Court upon such debt."

The first and second assignments of error raise the question of the jurisdiction of Courts of Bankruptcy under the law of 1898 over

a. Creditors who have proved their debts

b. Creditors who have not proved their debts.

To enjoin them from proceeding further on a judgment obtained without notice to the trustee and by default in a State Court, after the adjudication, and in a suit pending at the time of the adjudication and within a year thereof.

In the case at bar Silsby was not an "adverse claimant," and in determing whether or not he should be ordered to pay the money in his possession to the trustee, it was competent for the Court to cite in Flanders, Thayer and Rowley under powers conferred by Sec. 2, cl. 6 of Act of 1898, in order to completely determine the matter.

Bryan *v.* Bernheimer, 181 U. S. 188, 194, 197, 198.
Pirie *v.* Chic. T. & T. Co., 182 U. S. 438, 456.
In re Stokes, 106 F. R. 312.
In re Sheinbaum, 107 F. R. 247.

In the case at bar the creditor Thayer appeared and filed her claim, alleging and not waiving a security claimed.

This was a general appearance and gave to the bankruptcy court full power to deal with her claim and its security.

Act 1898, Sec. 2-7.
Pennoyer *v.* Neff, 95 U. S. 714.

In re Seebold, 105 F. R. 910, 914.

The security alleged was not *held* by the creditor within the sense of Sec. 57-h.

It is also submitted that Flanders as a creditor was a party and was before the court as a party, all creditors are parties.

In re Christy, 3 How. 292, 310.
Shawhan *v.* Wherritt, 7 How. 627, 643.
Bear *v.* Chase, 99 F. R. 920, 924.
Carter *v.* Hobbs, 92 F. R. 494, 497.
In re Cobb, 96 F. R. 821, 823.
Keegan *v.* King, 96 F. R. 758, 761.
In re Mason, 99 F. R. 256, 257.
In re Lesser, 100 F. R. 433, 438.
In re Fredenborg, F. C. 5075.
In re Lake, F. C. 7992.
Davis *v.* Anderson, F. C. 3623.
In re Davis, F. C. 3618.
Lee *v.* Savings Bank, F. C. 8188.

So that on notice his rights to alleged security might be determined on a petition in equity, ancillary to the bankruptcy proceedings.

White *v.* Ewing, 159 U. S. 36, 40.

The Court may compel a creditor to come in and prove and set out his security, and such security may then be passed on by the Court.

Bromley *v.* Smith, F. C. 1922.

"The fact of proof in bankruptcy defeats and annuls the suit and the attachment made therein."

Cook *v.* Coyle, 113 Mass. 252.

If the Court had jurisdiction of the parties it had jurisdiction of the cause.

Act 1898, Sec. 2. Sec. 2-15. Sec. 11.

A judgment obtained contrary to a prohibition is null and void.

Pennoyer *v.* Neff, 95 U. S. 714.

Federal courts will give relief against such a judgment.

Ins. Co. *v.* Hodgson, 7 Cranch, 332.

Where interests have been created for the purpose of preventing recovery relief will be granted.

Fosters Fed. Practice, Sec. 54 and cases cited.

Under the Massachusetts law bail is discharged in civil actions if the defendant is released from his liability to arrest by operation of law, and it was not necessary to surrender the bankrupt in order to maintain the claim of the estate upon the funds in the hands of Silsby.

Ingersoll *v.* Strong, 9 Met. 447, 453.
Collamore *v.* Fernald, 3 Gray, 318.
Carpenter *v.* Turrell, 100 Mass. 452.
Long *v.* Dickerson, 15 Blatch, 459.
Beers *v.* Haughton, 9 Pet. 329, 358.

Had the suits been pending they might have been stayed.

Hill *v.* Harding, 107 U. S. 631.
Boynton *v.* Ball, 121 U. S. 457.
In re Basch, 97 F. R. 761.
St. Cyr *v.* Daignault, 103 F. R. 854.
In re Neely, 108, F. R. 371.

As the suits had gone to judgment and execution had been issued but not satisfied, injunction was the appropriate and equitable relief.

THIRD ASSIGNMENT

"That the final judgment denied the jurisdiction of this court over controversies between the trustee and a third person in the possession of property alleged to belong to the bankrupt, it being also alleged that said third person has no beneficial interest in the said property but has the sole duty of paying or delivering it over in settlement of the debts of the bankrupt."

The third assignment of error is supported by the following cases:

Chapman *v.* Brewer, 114 U. S. 158, 172, 173.
Bryan *v.* Bernheimer, 181 U. S. 188.
Pirie *v.* Chic. T. & T. Co., 182 U. S. 438.
Wall *v.* Cox, 101 F. R. 403.
Hall *v.* Kincell, 102, 301.

FOURTH ASSIGNMENT

"That the final judgment denied the jurisdiction of this court to entertain jurisdiction of proceedings on a petition by a trustee in bankruptcy to recover property alleged to belong to the bankrupt, but held under a claim of lien or security by the bankrupt's creditor or by third party for the benefit of said creditor."

The fourth assignment of error seems to be supported by the text of the Bankruptcy Act and by the principles of construction heretofore adopted by this court, and which it is submitted must be taken to have been in the minds of the framers of the Act and have been the intent of Congress in passing the Act.

Sharpe *v.* Doyle, 102 U. S. 686, 689.
Feibelman *v.* Packard, 109 U. S. 421, 426.
In re Metzler (Blatchford, J.) F. C. 9512.

FIFTH ASSIGNMENT

"That the final judgment denied the jurisdiction of this court over this petition as it now stands on record."

The merits of the fifth assignment of error seem to require a brief review of some of the provisions of the Act and of some of the prior decisions of this court.

The constitutional power of Congress is to establish uniform laws on the subject of bankruptcies.

U. S. Con. Art. 1, Sec. 8.

The judicial power of Federal Courts extends to all cases in law and equity arising under the constitution or laws of the United States.

U. S. Con. Art. 3, Sec. 2.

And it is imperative that the whole judicial power necessary to enforce the Constitution and laws of the United States shall be invested in the Federal Judiciary.

Martin *v.* Hunter, 1 Wheaton, 304, 330, 331.

While by article 6 of the U. S. Constitution, the constitutional laws of the United States are made the Supreme law of the land and state court judges, bound by them, regardless of state constitutions and laws, still Congress can only vest the power to enforce them in the Federal Judiciary.

Story on Con. Sec. 1501, 1503.

And the grant given to the judiciary in the constitution is absolute and beyond the control of Congress.

Story on Con. Sec. 1594.
Ex parte Christy, 3 How. 292, 316.
Lathrop *v.* Drake, 91 U. S. 516, 518.

"It is a doctrine of law too long established to require a citation of authorities that, where a court has jurisdiction it has a right to decide every question which occurs in the cause."

Peck *v.* Jenness, 7 How. 617, 624.
Ogden *v.* Saunders, 12 Wheat. 213, 367.

Under the bankruptcy act the bankruptcy court has equity powers in matters within its jurisdiction. Sec. 2. It must collect the estate. Sec. 2-6, 7. Sec. 38-3. Sec. 47-2. And may appoint receivers. Sec. 2-3 and 5. May release bankrupt from custody of State Courts. Sec. 9. May stay suits in State Courts. Sec. 11. Can marshal securities. Section 5, G. Sec. 65, E. It may allow or disallow the claims of creditors. Sec. 2-2. Sec. 55-B. Sec. 57. Sec. 68. May order arbitration, litigation or compromise, and these provisions must certainly have reference to litigation pending in the State Courts as it is an unnecessary provision where cases are pending in the bankruptcy courts, it shows the intent of Congress that all litigation after the adjudication should be controlled by the bankruptcy court.

Section 26-A. Sec. 27. Sec. 57-H. Sec. 63-b. Sec. 11.

"Universally, after the law takes the bankrupt into its own hands his creditors are prohibited from suing."

Ogden *v.* Saunders, 12 Wheat. 213, 365.

May order conveyances by bankrupt or creditor. Section 7-4. Sec. 67-F. May pass on the nulity of judgments, etc., as preferences, uncontrolled by section 23.

Section 60. Sec. 67-A, B. C. D. F.

It is submitted that the word "transfers" as used in section 1-25, section 3-A, 1 and 2, section 3-b and section 60-a has a different and wider significance than the same word used in section 67-e, section 70, a-4, and section 70-e. This is evident from connecting with it in section 67-e the words "conveyances, assignments or encumbrances," words having no significance if the meaning is not different from the definition in section 1-25, and it is of acts of this more limited definition that section 67 provides that the trustees may reclaim and recover, and in section 70 that the trustee may avoid and recover. It is submitted that it is to such proceedings as these that the provisions of section 23-b are applicable. These seem to be the class of actions styled suits in section 46.

In the following sections the act refers to suits by trustees as distinguished from bankruptcy proceedings:

Section 11. Sec. 23. Sec. 46-a. Sec. 57-n. Sec. 67-e. Sec. 70-e.

Section 2-7 and 15 and section 47-2 and section 57-e, f, g, h, gives the bankruptcy court full and complete power to collect in the estates, to appoint trustees to act under the directions of the court, to determine whether preferences exist where the creditor comes into court to determine his securities, their amount and liquidation to determine the nullity of liens acquired within four months prior to adjudication and to make necessary orders to carry into effect the purposes of the act.

Now none of these latter are suits within the meaning of the act. They are the administrative acts of the court itself, in which the trustee plays no part, except that as an officer of the court, he calls to its attention such conditions as seem to him to show that the court should exercise the powers conferred, to make the will of Congress effective. He is as much an officer of the Court and a part of the Court as the referee.

It is clear that no separate suit is necessary in these matters, due notice under the bankruptcy proceedings is all that is required, Sec. 58 and 67, and apparently, this is because in these matters the rights of creditors only are being adjudicated and they are all drawn into court by the bankruptcy. They hold as security or lien, by virtue of the bankrupt's title, and under it they cannot dispute the bankrupt's title and hold their security, therefore the bankruptcy court may determine the fact of the lien or security, its amount, and order its liquidation.

Not so with conveyances, transfers, assignments, encumbrances, or liabilities for torts to properties, or conveyances in fraud of the statute of Elizabeth. These are not held as securities. The transfers are absolute, no title or right to redeem, remaining in the bankrupt and no debt against the bankrupt's estate remaining in the hands of his transferee. They clearly constitute a separate class, subject to the restrictions of Sec. 23-b.

The text of the act shows a clear cause for this distinction, by Sec. 17, a bankrupt is only discharged from a provable debt, by Sec. 57, secured or preferred debts, are only provable after liquidation of the security, and by Sec. 63, unliquidated claims are only provable after liquidation. Now it is impossible in the courts of the large cities or in any state in case an appeal is taken from the lower court, to try out such litigation within the space of one year from adjudication, provided either party is disinclined, so to do, yet, under the provisions of section 57-n, if such matters have not proceeded to final judgment within one year and one month or under the most favorable construction, one year and three months, the creditor is barred from proving his claim, and as the debt could not be proved under the act, the bankrupt will not be discharged therefrom. This construction seems to follow the proposition that the defendant by refusing consent can prevent the bankruptcy court from taking jurisdiction.

It is submitted that mere rights to recover property vesting in the Trustee under the provisions of section 70-a-4, 70-a-6, 70-e, must be pursued under the limitations of section 23, but that as a general proposition collecting and administering the other forms of property, mentioned in section 70, is within the jurisdiction of the District Court.

Section 23-a defines the jurisdiction of the Circuit Court solely. It is not until we reach section 23-b that we find any limitation upon the general powers of the District Court to draw to it all matters in controversy relating to the res being administered by it. This section permits all actions to be brought in the District Court by consent of defendant, a jurisdiction withheld from the Circuit Court, but if there is no consent all suits by the Trustee must be brought in the forum to which the bankrupt, prior to his adjudication, might have appealed.

The decision in Bardes *vs.* Bank, 178 U. S. 524, must be interpreted by the cases which it cites. Take the case of Morgan *vs.* Thornhill, 11 Wal. 65 and on page 75, we find that the decision governs only that class of cases or suits in which the action must be brought in the name of "one of

the two parties named in the clause" (U. S. R. S. Sec. 49, 79.) That is, in the name of the assignee or of the adverse claimant.

We find this distinction emphasized by reference to other portions of the act, in Sec. 63-b, the court is to direct the manner of liquidation of claims, it may determine them itself if there is no pending suit, or it may order the trustee to appear in a state court and defend a suit there pending.

Under Sec. 57, e, the court may determine the value of securities held and allow the rest of the claim, this imports also a power to determine whether there is any security at all, and if it has such power its decision must be res adjudicata if not appealed from, it would be a strange doctrine that with power to collect estates and determine controversies, the Federal Courts must implore the aid of State Courts to make their judgments effective.

Under Sec. 57, cl. f, objections to claims are to be heard and determined by the court, the objections that may be raised are, preferences, securities, counter claims and errors. Can it be said that the court shall determine that which it cannot determine? Can it be inferred that Congress intended to reduce the Federal Judiciary to moot courts?

Nor can it be argued from clause g, same section, that the purpose is to ascertain facts on which to found the rejections of claims alone, as under clause h, same section, the court has power to control the liquidation of the securities in any of the ordinary methods that it sees fit to direct.

The provisions of Sec. 67, e and f, clearly note the distinction drawn by Congress and outlined in Bardes *vs.* Bank in the matter of jurisdiction, under the sub-head of Liens Congress included every species of conveyance that might prove a fraud upon creditors, it then sub-divided them into those created by voluntary act and those created by adverse acts of courts, under color of local law.

True, the constitution of the United States enjoins upon State Judges the duty of upholding the paramount law of the land, but State Judges take their law from their own Supreme Courts and under these conditions there can not be uniformity in construing an act and the local forms and pro-

cesses may be such as to strip the Act of Congress of all efficiency and leave to the Bankruptcy Court nothing but naked rights incapable of enforcement, the property having been dissipated under local forms of law. It is submitted that Congress never intended to deprive the Federal Courts of the power to enforce a federal law, hence, Congress having incorporated in the bill the provisions set out in sections 9, 11, 57, 63, 67 and 70, inserted also the provision in Sec. 2-15, which powers may be enforced under the general provisions of Sec. 2 by the processes of a law or of an equity Court, and to make such procedure possible, and effective, Sec. 2, cl. 6, was enacted.

It is not contended that jurisdiction of actions by a trustee in his own name to recover debts or to avoid voluntary acts of the bankrupt enumerated in section 67-e is within the scope of these powers, that was settled in Bardes *v.* Bank, but that all matters on which parties may be brought into the bankruptcy proceedings on notice may be settled under these powers, as for example, all matters relating to claims of creditors set out in sections 57, 63 and 67, except 67-e, and it is familiar law, that, once the jurisdiction of a court, having equity jurisdiction attaches, that jurisdiction exists to the full determination of the whole controversy. The general observation of this court as to the purpose of the powers conferred on bankruptcy courts, in Ex parte Christie, 3 How. on page 314, holds good today.

In Bardes *v.* Bank this court cites the caution of Justice Curtis in Carroll *v.* Carroll against taking the opinion in Ex parte Christie as binding authority for more than the case presented for determination, and we receive this as an intimation that we are not to take the opinion in Bardes *v.* Bank as intended to be binding, except within the same limits. That case was an action to recover goods, voluntarily and absolutely, conveyed by the bankrupt, which conveyance was good except it contravened section 67-e. The decision was that on the facts presented there was no jurisdiction in the District Court. On the facts the case came clearly within section 67-e and not within section 60, as the bank was not a creditor, and therefore, it was not brought into court

by publication and notice in the bankruptcy proceeding. It had no provable debt; it had no power of election; it was paid in full.

See relating to creditors. Sec. 1-9 and 23. Sec. 18. Sec. 21, Chap. 6. Sec. 63 and 67.

All creditors are described as claimants, and their interests must necessarily be adverse to the estate. Sec. 21-c. Sec. 65-e. But they are not adverse claimants as defined in Bardes *v.* Bank, 178 U. S. 532, 538. And the power to bring in other parties is not incompatible with section 23-b.

Section 2-6, 5-c, 9-2, 11-a, 67-f.
White *v.* Ewing, 159 U. S. 36, 40.

And in the following cases it is apparent that creditors can be brought in on notice.

Sec. 21-c, 24-b, 39-4, 55, 58-b, 59-d, 67-f.
Ingersoll *v.* Strong, 9 Met. 447, 453.
Collomore *v.* Fernald, 3 Gray, 318.

It is respectfully submitted that when Congress determined to enact a bankruptcy law and created the District Courts, Courts of Bankruptcy, it did it for the reasons and purposes set out in Ex parte Christie, 3 How. 314. Uniformity, economy and despatch were clearly within its intent; the office of referee was created and invested with most of the administrative powers of the Court, nearly all the proceedings were required to be held in the county of the bankrupt with an appeal by certificate to the District Judge whose court was to be always open with full powers in term time or vacation, but in the wisdom of Congress referees were not constituted law courts with juries, nor equity courts, yet there must be more or less involved in the workings of a bankruptcy act, rights, which cannot be constitutionally passed upon except by a jury or by a judge constitutionally qualified, and holding office during good behavior. (Con. U. S. Act 3, Sec. 1.) These rights are clearly set out in

Marshall *v.* Knox, 16 Wal. 551, 556, and hence in order that oppression might not be done, that defendants might not be put to great expense of travel and witnesses, compelled to attend a District Court at the farther end of the district, Congress enacted that except by consent these suits to "recover" to "reclaim" should be brought in the State Courts.

Experience under the act has demonstrated the wisdom of the provision, for a very large number of suits to recover have been brought without any foundation except the suspicions of inexperienced trustees, backed by the fact that the litigation was paid for out of a fund, and that the trustee's lawyer had spare time not otherwise required in his practice.

But on the other hand it seems that Congress intended to have the District Court settle, and settle within one year, every question connected with a creditor's claim and his security, and if such matters must be settled within a year, only the District Court can do it in many sections of the country, and especially in those sections most rich and most populous where the bankruptcy cases are largest in number and amount.

In Suffolk County, Massachusetts, a jury case involving $2,000 or more cannot be reached short of eighteen months to two years, and while a smaller case could be tried in three or four months, an exception to the Supreme Court would delay final judgment beyond the term allowed by the bankruptcy act for proving the claim, therefore it seems not to be unreasonable to suppose that the framers of the act knew of and had these conditions in mind and only intended that suits against third parties, not creditors, strangers to the bankruptcy proceedings, should go to the State Courts, but that everything pertaining to bankrupt and creditor, including all accountings and securities between them, should be exclusively heard and determined by the District Court, except that that court ordered the question tried out in a pending suit.

This view seems to be supported by the prohibition upon trustees venturing into pending suits except by order of the court.

Price *v.* Price, 48 F. R. 823.
Sec. 11-b.
In re Klein, 97 F. R. 31.
Bear *v.* Chase, 99 F. R. 920.

And this is particularly true where the litigation in the State Court is practically ended.

Traders Bank *v.* Campbell, 14 Wal. 87, 95, 96.
Norton *v.* Switzer, 93 U. S. 355, 364.

It seems to the appellant that the subject matter of his petition to the District Court did not constitute a suit within the meaning of the act, but only an ancillary proceeding and that the parties summoned in were not adverse claimants within the words of the Act of Congress or within its intent, or within the prior decisions of this Court, but that the matter involved was purely administrative to carry into effect the purposes of the Act, and that the District Court had jurisdiction and full power to make any orders therein, according to the usual practice of equity courts, which in its judgment the facts might seem to warrant.

The appellant respectfully submits that under the Bankruptcy Act the District Court of Massachusetts has jurisdiction to hear and determine the matter set out in the record, and to make such orders as may be necessary for the enforcement of the provisions of the Act.

H. J. JAQUITH
pro se